



The Mediating Effects of Corporate Social Responsibility Disclosures on the Relationship Between Corporate Governance and Financial Performance

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ABSTRACT

Purpose: This study examined the mediating effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance.

Methodology: The current study methodologically reviewed the relevant studies concerning the effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance.

Findings: The study reviewed the literature, and results revealed a mixed impact on mediating effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance.

Practical Implications: findings will significantly impact developing countries on how to deal with corporate social responsibility disclosures, corporate governance and financial performance.

Originality/Value: The study was conducted in a new setting where fewer empirical studies were done to review the mediating effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance.

1. Introduction

Several debates have occurred over the last several decades regarding the analytical aspect of firms' financial performance announcements on their market value and financial returns (Araya, Dahalan, & Muhammad, 2022). Simultaneously, improved corporate governance practises are required to meet the ethical standard of finance management (Baydoun, Maguire, Ryan, & Willett, 2013). Nonetheless, the reputation of corporate governance was severely harmed at the turn of the century after so many companies experienced meltdowns due to management deceptions, misbehaviour, and negligence, causing enormous damage to shareholders' capital (Baker & Anderson, 2010). Over time, these issues have become a challenge in countries. For most, corporate governance has been a significant concern for MENA investors (Shehata, 2015). Corporate scandals in various countries have piqued the interest of global investors in corporate governance. Enron, for example, and the negative publicity surrounding its senior executive pay, have "increased society's expectations about companies' environmental, social, and ethical responsibilities in the United States" (Chan, Watson, & Woodliff, 2014). As a result, corporate governance is expected to impact corporate social responsibility (CSR) disclosure. Separation of ownership and control is shared in common law countries such as the United Kingdom; however, ownership concentration remains high in many countries, particularly in Continental Europe, Latin America, East Asia, and Arab countries (Alkahtani, 2021). Emerging-market firms are more likely to have a concentrated ownership structure, which can result in a conflict of interest between non-controlling (minority) and majority shareholders (Din, Khan, Khan, & Khan, 2021). On the other hand, stakeholders' perceptions of a company's success are shaped by its financial performance and attitude towards social issues and surroundings (Kirana & Prasetyo, 2021). As a result, ownership structure and CSR disclosure are expected to impact financial performance.

CSR disclosure is communicating the social and environmental consequences of an organisation's economic actions to specific interest groups within society (Razek 2014). Traditionally, CSR researchers have concentrated on companies in developed countries such as the United States, the United Kingdom, Australia, and New Zealand. However, as developing countries shift towards capitalist orientations, there is growing interest in understanding the phenomenon (Tilt, 2016). According to previous research, poor corporate governance leads to poor firm operations and losses for investors (Baydoun et al., 2013). Multidisciplinary political science, accounting, finance, economics, and even philosophy researchers have expressed an interest in corporate governance (ElGammal, El-Kassar, & Messarra, 2018). Corporate governance is an essential aspect of the financial market. It improves market functioning while contributing to the firm financial performance by contributing efficiently, as society requires. As a result of the potential for significant adverse external effects on the public, understanding the relationship between corporate governance and CSR disclosures is critical for firms (Chan et al., 2014). As a result, an increasing number of businesses are engaging in CSR activities that provide additional societal and environmental information, making CSR disclosures one of the most critical areas of research for accounting students (Tilt, 2016). Furthermore, asset prices are difficult to reconcile with underlying

economic conditions due to the history of capital market booms and busts. For instance, (Araya and Miras, 2015; Semmler, & Bernard, 2012; Araya, Dahalan, & Muhammad, 2021b). The asset classes are the market system's most complex and essential elements, valuable distributed resources that meet basic human needs, the foundation of many different types of businesses, national wealth, and government revenue (Araya, Dahalan, & Muhammad, 2021a). CSR disclosure has become an increasingly important component of asset classes due to its impact on firms' ethical standards. As a result, the goals are to investigate the effect of corporate governance board independence, managerial ownership, or family ownership on CSR disclosures and the financial performance of publicly traded companies. The rest of the article is organised as follows: Section 1.2 below focuses on Corporate Social Responsibility. In section 3, the theoretical approaches are followed by the conceptual framework in section 4. the conclusion is provided in section 5.

2. Overview of Corporate Social Responsibility

Recognising the importance of corporate social responsibility was a difficult but necessary choice. It necessitates a variety of tactics with varying meanings, which can lead to disputes. This is partly due to imbrications and mix-ups using the same terminology and definitions as in other areas. Examples include business ethics, ethical performance, ethical standards, etc. As a result, CSR has evolved into a broad concept that describes how businesses engage in positive social activities that go above and beyond their legal obligations (Kim, Lee, & Roh, 2020). These measures incorporate economic, social, and environmental goals into the company's objectives (Fandos-Roig, Sánchez-Garca, Tena-Monferrer, & Callarisa-Fiol, 2021). Because it is linked to the levels of integrity with which a company manages or directs itself, CSR is defined and conceptualised as a desirable strategic tool for long-term development (Fandos-Roig et al., 2021). Several theories exist, however, to support corporate social responsibility as a framework for efficient and adequate corporate performance and disclosures; ideas relevant to the current study will be explained in the following section. Thus, the challenge for businesses is understanding how corporate social responsibility is informally built in a specific setting rather than identifying its importance. By defining what sustainable development means to a corporation, corporate social responsibility is incorporated into business plans and integrated into how a company operates (De Wit, Wade, & Schouten, 2006)

"Sustainable development considerations must be hardwired into existing structures if they are to be managed like any other business activity" (De Wit et al., 2006). Full disclosures of corporate social responsibility aid in firm direction and regulation, and thus management is expected to encourage corporate social responsibility (Jizi, Salama, Dixon, & Stratling, 2014). Organisational ethics and corporate social responsibility are now required for businesses to compete for more market share. On the one hand, they would require firms to retain exceptional and skilled employees; on the other hand, they would assist businesses in addressing and meeting the potential of their clients (Ur Rehman et al., 2020). Indeed, many companies have published evidence of their ethical standards in corporate social responsibility disclosures (Dhaliwal, Li, Tsang, & Yang, 2014). As a result, the most systematic approaches to the concept of corporate social responsibility denote the organisation's desire to discover asymmetry between monetary, ecological, communal, and permissible necessities, as perceived by shareholders and the general public, as a way of being for the company (Badulescu, Badulescu, Saveanu, & Hatos, 2018). More companies intend to "do the right thing" regarding corporate social responsibility and governance (Mason & Simmons, 2014). Recognising interdependence, identifying shared benefits, and pursuing corporate social responsibility among diverse social performers are all part of this (Jamali, 2011).

3. Theoretical Framework

Several theories backed corporate social responsibility as a framework for assessing ethical principles in business. These theories are agency and stakeholder theories, described in the following sections.

3.1 Theory of Agency

Because it is appropriate for situations in which one party, or the principal, has been designated as having control and decision-making authority over specific duties delegated to another party or agent (Fayezi, O'Loughlin, & Zutshi, 2012). Many different studies have made extensive use of agency theory. The seminal contributions of scholars have significantly increased our understanding of how agency theory updates financial communications (Swanson & Goel, 2017). Agency theory has been used in academia to illuminate communications in a variety of fields, including economics and finance (Sappington, 1991), information systems (Mahaney & Lederer, 2003), and management (Mahaney & Lederer, 2003; John & Senbet, 1998). However, the theory has been criticised in recent years. Opponents of agency theory argue that public regulations outside the principal-agent contract can impact regulatory agent performance, which can be firm-specific to the company's situation (Wiseman, CuevasRodrguez, & Gomez-Mejia, 2012). On the other hand, academics argue that a firm-specific framework limits core corporate governance ideas and recommendations within and across countries (Wiseman et al., 2012). Nonetheless, observers have advocated for distinct governance representations characteristic of the dominant formal setting and the defined national setting under consideration (Bruce, Buck, & Main, 2005). The influence of broader societal factors on the relationship between manager and agency has been acknowledged (Wiseman et al., 2012). According to Wiseman et al. (2012), agency theory applies to various situations.

3.2 Stakeholder Theory

Stakeholder theory has dominated academic discussions (dialogue) in management fields (Harrison & Wicks, 2013). This theory has been expanded to include corporate social responsibility as an environmental context component, such as the sustainability of corporate governance characteristics and how corporations conduct their business from a legal and ethical standpoint (Kujala, Lehtimäki, & Freeman, 2019). Stakeholder engagement has grown in popularity in business and society research and related fields of study. However, while research on stakeholder engagement has given the concept prominence and theoretical and practical relevance, the research has resulted in a heterogeneous, if not fragmented, research area (Kujala et al., 2019). The debate over where corporate accountability ends and regulatory accountability begins can be traced back to the 18th century when opposing arguments about wealth and control were made (Djelic & Etchanchu, 2017). This argument was modernised by (Friedman, 2007), who argued that corporate executives' only responsibility is to their employers, who are the firm's shareholders. However, Foote, Gaffney, & Evans (2010) contended that the corporation is accountable to groups other than shareholders and those with a vested interest in its actions. Stakeholder theory has been expanded to include owners, employees, suppliers, customers, lenders, investors, and the local community or society in which the corporation operates to increase owners' capital and increase value creation for owners (Kujala et al., 2019). The maximisation of shareholder value does not contradict the stakeholder perspective. Users can interpret it instead as a strategy for increasing shareholder value, which could be extended to environmental settings and other firm characteristics such as corporate social responsibility and corporate ethics (Kujala et al., 2019).

4. Conceptual Framework

This section focuses on hypothesis testing and model building. It explains the statements of the hypothesis. It describes the assumptions of the models derived from the research framework of the current study. Further, the section describes the formulation of the conceptual framework dimensions of corporate governance and CSR disclosures concerning financial measures. These complete the model frameworks of the research. The diagram below provides the association among the research variables.

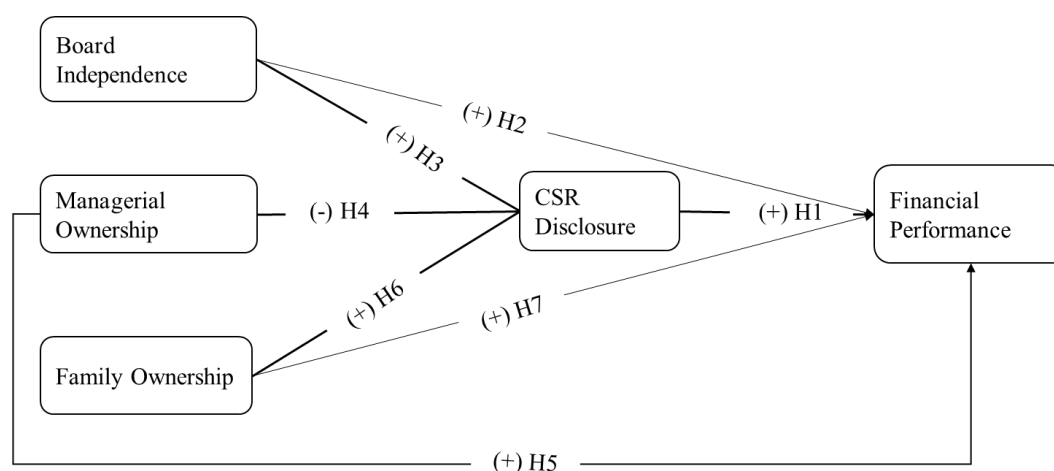


Figure: 1 Conceptual Framework of the Study

4.1 Relationship between Financial Performance and CSR disclosures

The stock price basis (the market basis) investigates how much a company's socially responsible behaviour results in higher stock returns (Chang, Lin, Tsai, Wang, & Huang, 2021). The majority of the studies use accounting-based metrics to evaluate business financial performance. According to some academics, CSR has a positive impact on financial performance. For example, Kim, Cho, & Park, (2019) investigated whether CSR disclosures affect the relationship between CSR success and financial performance. The findings show that CSR disclosure helps companies reduce economic costs by lowering the discount rate for investors, thereby improving financial performance. Cho, Chung, & Young (2019) gathered 191 sample enterprises listed on the Korea Exchange to investigate the impact of CSR on financial performance. They discovered a partially positive relationship between CSR and financial success as measured by return on assets. Uadiale & Fagbemi, (2012) investigated the impact of CSR activities on financial performance as measured by return on equity (ROE) and return on assets (ROA) using a sample of 40 audited financial statements of Nigerian listed firms (ROA). According to their findings, CSR positively and significantly impacts various financial indicators.

However, some empirical research suggests that unobservable organisational traits influence CSR rather than financial performance (Garcia-Castro, Ario, & Canela, 2010). Margolis & Walsh (2003) examined 18 previous CSR studies and

discovered that only 53% showed a positive correlation between CSR and financial success, indicating an ambiguous relationship between the two variables. Cho et al. (2019) discovered that previous empirical studies on the impact of CSR on financial performance produced contradictory results. Furthermore, Cherian et al., (2019) examined the financial impact of CSR reporting using secondary data from 50 Indian manufacturing enterprises from 2011 to 2017. They discovered that declaring the CSR act has a negative impact on the value of a company. Those who believe that CSR and financial success are unrelated argue that a higher level of CSR places a greater economic burden on the company than a lower level of CSR (Aupperle, Carroll, & Hatfield, 1985). Some academics, however, argue that CSR and financial performance are unrelated. According to Waddock & Graves, (1997), Negligible results may indicate that many variables in the link between social and financial performance cause their relationships to be coincidental. This study hypothesises that:

H1: There is a significant positive relationship between CSR disclosures and financial performance of firms in developing countries.

4.2 Effect of Board Independence on Corporate Social Responsibility Disclosures and Financial Performance

There are boards in every company, which are recognised as the main body that decides the firm's direction. Groups of decision-making bodies or teams influence decisions within the firm, and thus the decision is influenced by different behaviour (Adams, 2017). There is evidence that if the board is composed of a majority of independent individuals, it will perform better (Bhojraj & Sengupta, 2003). Larger boards are more likely to reinforce the influence of CSR on financial results with better-addressed CSR and more tools provided for consulting and tracking roles. As a larger number of people can be divided into the workload of monitoring managers, larger boards are more likely to reinforce the influence of CSR on financial results with better-addressed CSR. More tools provided for consulting and tracking roles are more likely to reinforce the influence of CSR on financial results with better addressed (Rossi et al., 2021). According to previous research, large boards have a broader range of skills and experience, which benefits a company's reputation and image (Jizi et al., 2014). Large boards tend to have directors with diverse backgrounds and relationships that enable organisations to project their image, and directors have a reputation that helps extend the corporation's positive esteem. Thus, successful companies had larger boards than firms that did not survive (Orozco, Vargas, & Galindo-Dorado, 2018). Giannarakis (2014) investigated the link between board independence and CSR disclosure in the USA companies. His research found significant and positive links between board independence and CSR disclosures. Khan (2010) investigated the association between board independence and CSR disclosures in Bangladeshi businesses. The study's sample included all private commercial banking for the fiscal years 2007 and 2008. His research found that board independence significantly and positively impacts CSR disclosures. From 2007 to 2011, (Das, Dixon, & Michael, 2015) investigated the relationship between board independence and CSR disclosures on 29 public banks in Bangladesh. The findings of their study also show a significant and positive relationship between board independence and CSR disclosures. Khan, Muttakin, & Siddiqui (2013) investigated the extent to which board independence influences CSR disclosures and discovered that board independence has a significant and positive impact on CSR disclosures. Lagasio & Cucari (2019) used meta-analysis to examine the relationship between board independence and company voluntary disclosure, and they discovered that board independence significantly improves voluntary disclosure.

Gerged (2021) investigated whether internal corporate governance mechanisms influence CSR disclosure in emerging economies. Using a sample of 500 firm-year observations, the study employs a novel linear panel quantile regression model to investigate the relationship between board independence and CSR disclosures in Jordan. This technique was supplemented with a two-step dynamic generalised method of the moment model to overcome potential endogeneity issues. The study results suggested that board independence has positive associations with CSR disclosures. According to Ntim & Soobaroyen (2013), independent board members increase management supervision by allowing executives to participate in long-term CSR initiatives that may benefit their companies' financial success. They are better at involving a wide range of stakeholders and devising sensitive strategies that balance short- and long-term goals, positively moderating the relationship between CSR and financial performance (Liao, Chen, & Zheng, 2019). Based on past studies, therefore, this study hypothesises that:

H2: There is a significant positive relationship between board independence and financial performance of firms in developing countries.

H3: There is a significant positive relationship between board independence and corporate social responsibility disclosures of firms in developing countries.

4.3 Effects of Managerial Ownership on Corporate Social Responsibility Disclosure and financial performance

A theoretical suggestion has been made regarding the role of managerial ownership in CSR disclosures. According to (Eisenhardt, 1989), management influences the allocation of resources among diverse shareholders in ways that ensure shareholder support. As a result, aligning management's interests with those of the owners, such as offering stock to executives, is an effective way to alleviate agency problems. If management owns a significant portion of a company, there is a chance that they will make decisions that maximise shareholder value (Denis, Denis, & Sarin, 1999). As a result of these incentives, if social responsibility actions increase the corporation's value, stock ownership may increase management motivations to engage in CSR disclosures.

A high level of managerial ownership fosters agency issues and information asymmetry (Sufian & Zahan, 2013). In 2006, Oh, Chang, & Martynov (2011) investigated the relationship between managerial ownership and CSR disclosures. Their sample size was comprised of 118 large Korean corporations. The findings of their study revealed a significant and inverse relationship between managerial ownership and CSR disclosures. Soliman, El Din, and Sakr, (2013) Investigate the link between managerial ownership and CSR disclosures. From 2007 to 2009, the sample size was 42 highly active Egyptian firms. Their research found that managerial ownership significantly and negatively impacts CSR disclosures. (A. Khan et al., 2013) Investigating managerial ownership's effect on CSR disclosures and discovering a significant and negative effect. Consistent with the entrenchment model's hypothesis, a large body of literature argued that higher managerial shareholding allows managers to exercise discretion over firm policies (Sani, 2020). According to these studies, a higher level of managerial ownership leads to managers' excessive perquisite consumptions and agency conflicts, negatively influencing company performance (Shan, 2019). This could be due to the different levels of disclosure, as their study results for export-oriented industries demonstrated a significant and positive impact. Albassam (2014) investigated the relationship between managerial ownership and CSR disclosure in the family-concentrated ownership structure of KSA firms. His findings revealed a significant, inverse relationship between managerial ownership and CSR disclosures. Gerged (2021) investigated the relationship between managerial ownership and CSR disclosure in Jordan. According to the study's findings, there is a negative relationship between managerial ownership and corporate social responsibility disclosures. The agency theory documented two opposing viewpoints on the effect of managerial ownership on firm performance: the alignment hypothesis and the entrenchment approach (Sani, 2020). The alignment perspective, in particular, believes that managers have less incentive to divert resources to their benefit when they own a significant portion of the equity in the firms they manage. As a result, managerial ownership may help align the interests of shareholders and managers, improving firm performance (Sani, 2020). Most of the literature found negative effects of managerial ownership on CSR disclosures. Therefore, this study predicts that the impact of managerial ownership on CSR disclosures and financial performance will be negative, and thus the following hypothesis is formulated:

H4: There is a significant and negative relationship between managerial ownership and corporate social responsibility disclosures of firms in developing countries.

H5: There is a significant and negative relationship between managerial ownership and financial performance of firms in developing countries.

4.4 Effect of Family Ownerships on Corporate Social Responsibility Disclosures, financial performance

Regarding the relationship between family-owned businesses and CSR disclosures, researchers contend that family-owned businesses are more socially responsible and prefer to disclose and be accountable (Habbash, 2016). According to the literature, family-owned businesses are more likely to support corporate social responsibility initiatives. However, these companies are more willing to disclose information voluntarily than non-family-owned businesses (Habbash, 2016). Khan et al. (2013) examined the extent of family ownership's impact on CSR disclosures. Their findings indicated that family ownership significantly and positively affected CSR disclosures.

Albassam, (2014) investigated the relationship between family-owned businesses and CSR disclosures in KSA firms with a family-concentrated ownership structure. Between 2004 and 2010, 560 firm-year observations were collected from the annual reports of the sampled firms from a balanced panel of 80 publicly traded companies. His research discovered a significant and positive link between family ownership and CSR disclosures. However, Haniffa, & Cooke, (2005) discovered evidence that family-owned businesses were more reluctant to disclose information voluntarily than non-family-owned businesses. Due to the potential cost of disclosing, the family's firms may not engage in extensive CSR disclosures (Soliman et al., 2013). The evidence on agency costs for family-owned businesses is mixed; some studies found that family-owned businesses have fewer agency problems and higher performance; however, other studies discovered that family ownership increases agency problems and lowers firm performance (Srivastava & Bhatia, 2020). According to evidence in the literature on agency and stewardship theories, family ownership is expected to improve a firm's financial performance. Therefore, it is hypothesised that:

H6: There is a significant and positive relationship between family ownership and corporate social responsibility disclosure of firms in developing countries.

H7: There is a significant and positive relationship between family ownership and the financial performance of firms in developing countries.

5. Conclusion

Research on disclosure's effects on corporate social responsibility growth has been scant in developing countries. This may be because researchers have been unable to work with the current definitions of corporate social responsibility disclosures. Maybe due to the newness of the concept of corporate social responsibility disclosures to the developing countries as very few countries promote corporate social responsibility is still institutionalised in the region. The main objective of this study was to investigate the mediating effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance. To accomplish this goal, the researcher reviewed the mediating impact of corporate social responsibility disclosures on the relationship between corporate governance and

financial performance. According to the study findings, there are mixed results. The study findings revealed a positive/negative relationship regarding the mediating effects of corporate social responsibility disclosures on the relationship between corporate governance and financial performance. Therefore, the study results support the question of whether corporate social responsibility disclosures have mediating effects on the relationship between corporate governance and financial performance.

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